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IN THE

Supreme Court of the United States

OCTOBER TERM, 1971

No. 71- 71-414

VULCAN MATERIALS COMPANY, *Petitioner,*

v.

UNITED STATES OF AMERICA, *Respondent.*

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

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PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

OPINIONS BELOW

The opinion of the Court of Appeals is not yet officially reported.

It is unofficially reported at 27 AFTR 2d 71-1488 and at 71-1 USTC ¶ 9449. The opinion of the District Court is officially reported at 308 F.Supp. 53 and is

unofficially reported at 25 AFTR 2d 70-443 and at 70-1 USTC ¶ 9,189.

The date of the judgment sought to be reviewed and the time of its entry was May 28, 1971. A petition for rehearing was timely filed and was denied on June 25, 1971. The statutory provision believed to confer on this court jurisdiction to review the judgment in question by writ of certiorari is Title 28, Section 1254(1) U.S. Code (62 Stat. 928).

QUESTIONS PRESENTED

1. Whether the surviving corporation in a corporate merger should be denied the right to deduct its own net operating loss carryover because of the provisions of Section 269 of the Internal Revenue Code of 1954 where, after the merger, the stockholders of such loss corporation continued to own more than fifty percent of the outstanding stock of such surviving corporation?

2. Whether, upon the consummation of a corporate merger of a Delaware into a New Jersey corporation, the non-surviving Delaware corporation is entitled to deduct, as losses, pursuant to Section 165 of said 1954 Code, the unamortized expenses of organization and reorganization of itself and predecessor corporations not deductible in prior years?

3. Whether, upon the consummation of a corporate merger of a Delaware into a Delaware corporation, the non-surviving constituent corporation is entitled to deduct, as losses, pursuant to Section 165 of said 1954 Code, the unamortized expenses of organization and reorganization of itself and a predecessor corporation not deductible in prior years?

STATUTES INVOLVED

The federal statutes involved in this case are copied in the Appendices, pp. 30a-37a.[1] All are parts of the United States Internal Revenue Code of 1954 (the "1954 Code") and are Sections 63 (68 A. Stat. 18) and 161 (68 A. Stat. 45) and portions of Sections 165 (68 A. Stat. 49), 172 (68 A. Stat. 63), 269 (68 A. Stat. 80), 381 (68 A. Stat. 124), and 382 (68 A. Stat. 129), all as they existed in 1954 and in 1957, respectively. Sections 381 and 382 are not deemed to be directly involved, but may have to be consulted in aid of the construction of Sections 172 and 269, in the aspects here involved. Portions of the laws of the State of New Jersey, Delaware and Illinois which are deemed to be relevant, are copied on pp. 21a-27a, 29a and 30a.

STATEMENT OF THE CASE

The facts which we believe are relevant to the questions above are stated below. Except as hereafter shown, all the facts were stipulated, p. 3a.

By this petition, the petitioner seeks to have this Court review the decisions of the Court of Appeals for the Fifth Circuit in two cases in both of which the petitioner was the appellant. They were numbered 30,116 and 30,117, respectively, in the Court of Appeals and are so designated herein.

The petitioner (hereafter generally called "Vulcan") is a corporation organized under the laws of New Jersey[2] and is the surviving corporation in a series

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[1] Page references followed by "a" are to pages in the appendices.

[2] The opinion of the Court of Appeals does not disclose that Vulcan is a New Jersey corporation, though the fact could control the decision. It is shown in the opinion of the District Court, 308 F.Supp. 54.

of corporate statutory mergers which were consummated as follows: Effective December 31, 1953, the Consumers Company ("Consumers") and Frontier Chemical Company ("Frontier"), both Delaware corporations, were merged into Follansbee Steel Corporation ("Follansbee"), also a Delaware corporation, under the laws of Delaware. Follansbee was the corporation surviving such merger, pp. 44a, 54a. In the course of this merger, the "1953 merger," Follansbee's name was changed to Union Chemical & Materials Corporation, and it is hereinafter sometimes referred to as Follansbee-Union Chemical. This is the "1954 merger."

On December 31, 1957, Follansbee-Union Chemical and Lambert Brothers, also a Delaware corporation, merged into Vulcan under the laws of Delaware and New Jersey, with Vulcan as the surviving corporation. This is the "1957 merger." Each of the above-mentioned mergers constituted a reorganization within the meaning of Section 368 (a) (1) (A) of the 1954 Code.

Throughout this petition, we use the term "merger" in what we understand is the technical sense. Paraphrasing the definition by the Court of Appeals, a statutory merger effects a combination of two or more corporations, "with the of the corporations sur-

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[1] In several expressions the opinion of the Court of Appeals may appear to indicate that Follansbee-Union Chemical was not the same corporation as Follansbee. But as the Court of Appeals calls the transaction a "merger" and in its definition of a statutory merger says that "one of the corporations continues as the same entity it was before the transaction" (p. 7a), the opinion apparently properly refers to Follansbee-Union Chemical as "the surviving corporation." (pp. 4a, 7a).

tinuing as the same legal entity it was before the transaction," p. 7a.

Each of these cases involved an appeal from a judgment of the District Court for the Northern District of Alabama (Southern Division) in an action by Vulcan against the United States for the recovery of income taxes paid by Vulcan, or a predecessor thereof, in respect of the income tax liability of a predecessor in the series of mergers described above. In each case, jurisdiction of the District Court was invoked under Section 1346(a) of Title 28 of the United States Code (62 Stat. 939). The right of the petitioner to maintain these actions was not challenged and, in respect of any tax paid by a predecessor, is supported by *Seaboard Airline Railway* v. *U. S.*, 256 U.S. 655 (1921).

These cases were originally designed to procure deductions of organization and reorganization expenses upon the consummation of each of the 1954 and 1957 mergers, hereafter called only "organization expenses." The plainer case appears to be presented with respect to the 1957 merger, for there Delaware corporations were merged into a New Jersey corporation. However, in order to defeat the claim with respect to the 1957 merger, the Government denied the net loss carryover. Therefore, this issue must also be considered by the Court.

No. 30,116 involves the income tax liability of Consumers for its taxable year which began on January 1 and ended on December 23, 1954, the effective date of its merger into Follansbee-Union Chemical. This case presented only the question of the deductibility of organization expenses of Consumers and its predecessor. No. 30,117 involves the income tax liability

of Follansbee-Union Chemical for its taxable year which began on March 1, 1957, and terminated on December 31, 1957, the effective date of the merger into Vulcan, its "taxable year 1957." No. 30,117 involves what is herein called the "net loss issue," and also issues respecting the deductibility of organization expenses of Follansbee and its predecessor, Follansbee Brothers Corporation, and such part of the organization expenses of Consumers as are not allowable as deductions in No. 30,116.

While the cases constituted separate suits, they were consolidated for trial and hearing in the District Court and for oral argument in the Court of Appeals, and a single opinion was rendered in each court. If the deduction of the organization expenses of Consumers is denied in No. 30,116, they may be allowable as deductions in No. 30,117. The facts that the deductibility of organization expenses upon the consummation of a statutory merger is involved in each of Nos. 30,116 and 30,117 and that those of Consumers may be allowable in either case are the occasion for seeking review of both thereof by this petition. This procedure is permitted by paragraph 5 of Rule 23.

There was no oral testimony, but there were only stipulations and exhibits. One of the exhibits was the notice of the special meeting of the stockholders of Follansbee called to be held on October 27, 1957, and the Proxy Statement attached thereto. The others were a copy of the 1957 merger agreement and a certificate by the Secretary of State of New Jersey that, in the 1957 merger, Vulcan did not procure any credit for any fees paid to the State of Delaware by either Follansbee-Union Chemical or Lambert Brothers.

The Net Loss Issue

Vulcan could recover in No. 30,116 for 1954 even though it loses on the net loss issue in No. 30,117, but it is not entitled to recover in No. 30,117 if it should lose that issue. As the result of operations and the sale of operating assets, Follansbee incurred a net operating loss of some $6,000,000 in its taxable year that began January 1, 1954. Carrybacks to prior years were allowed as deductions under Section 172 of the 1954 Code. The remaining portion of the 1954 net operating loss was deducted by Follansbee-Union Chemical as carryovers to later taxable years. The final portion was originally allowed as a deduction for the taxable year 1957, but was disallowed in the denial of the refund claim. This is the only deduction which is challenged in reliance on Section 269 of the 1954 Code.

Under the contract for the sale of Follansbee's operating assets, and after deduction of expenses and a cash refund, and provision for additional expenses, losses, etc., Follansbee-Union Chemical was left with net current or liquid assets in the sum of approximately $8,500,000. Follansbee's Controller estimated its tax loss carryover at $4,700,000 and the value thereof at $2,300,000. Certain exchange ratios were suggested by him. These were followed in the 1954 merger agreement, with the following results.

The stockholders of Follansbee retained the 464,469 shares of its common stock which they owned immediately prior to the merger and received the same number of shares of Follansbee-Union Chemical's 5% Cumulative Preferred Stock of the par value of $5.00 per share. This was the entire issue thereof, and it

was limited as to voting power. All that the stockholders of both Consumers and Frontier together received initially, and later, as a result of the merger, was the total of only 449,195 shares of Follansbee-Union Chemical's common stock.

Thus, those who were the stockholders of Follansbee immediately before the 1954 merger continued to own more than 50% of each of the voting stock and of the fair market value of all outstanding stock, of the single corporate taxpayer, Follansbee-Union Chemical, that was outstanding immediately after the consummation of the 1954 merger. The Court of Appeals treated the interest of the old Follansbee-Union Chemical stockholders as being 57% of the whole, to which we take no exception, e.g., pp. 11a, 14a.

In its dealing with the requirements of Section 269 that the "principal purpose" of the transaction described in either clause (1) or (2) is the "evasion or avoidance of Federal income tax," the Court of Appeals concluded that Follansbee had converted its assets to cash at some time before the stockholders' meeting and made other comments with respect to the relationship between the sale of Follansbee's assets and the merger. The first statement is altogether incorrect, and some comments are either erroneous or misleading. These errors are not presented as a direct issue and therefore the demonstration thereof is shown only at the end of the appendices (p. 44a).

Organization Expense Issues

The amount claimed in No. 30,116 for 1954 in respect of the organization expenses of Consumers is $168,890.91, with interest paid and allowable. Vulcan itself paid most of this tax, but some had been paid

by Follansbee-Union Chemical, as transferee of Consumers.

From 1933 through 1937, various expenditures were made by Consumers (called "Delaware" in the stipulation) and its predecessor (called "Illinois" therein) with respect to the reorganization of the predecessor under Section 77(b) of the Bankruptcy Act and the organization of Consumers. Each expenditure was capital in nature and not deductible when paid or incurred. Each item and a brief description thereof were stipulated. The total was $293,712.77. They included payments to the trustees in bankruptcy, committees for creditors, and stockholders, and their counsel and the amounts paid to the persons or firms named in respect of the items which are copied on p. 43a, ff.

The Court of Appeals thought that the $3,209.34 paid to the Secretary of State of Illinois was not sufficiently identified as the expense of qualifying Consumers to do business in Illinois, but stated that such an expense might be deductible, footnote 4, p. 9a.

Relevant portions of the 1957 Merger Agreement provide, in part, that Vulcan, "The Surviving Company shall be governed by the laws of the State of New Jersey," and, after reference to the Delaware statutes, that: "Thereupon, the said corporations shall be one corporation, which shall be Vulcan, and the separate existence of Union (i.e., Union Chemical) and Lambert shall cease."

In addition to any organization expenses that are not allowed in No. 30,116, Vulcan claims the following described Follansbee organization expenses. Follansbee Brothers Company, predecessor of Follansbee, was

a corporation organized under the laws of Pennsylvania. Follansbee was organized on March 29, 1937, to effect the plan of reorganization of such predecessor in proceedings under Section 77(b) of the Bankruptcy Act then in effect. Follansbee assumed payment of all liabilities and obligations of Follansbee Brothers Company not affected by the plan of reorganization. These included all allowed expenses of reorganization and administration.

The amounts of the organization and reorganization expenses so paid are shown in Sched. II to the complaint and aggregated $307,230.50. $8,474.03 thereof represented expenses for listing Follansbee's stock on the New York Stock Exchange. In addition to compensation for the trustees in bankruptcy and their counsel, such expenses also included compensation for committees representing bondholders, unsecured creditors, preferred and common stockholders and their counsel. In 1946, the Sheet Metal Specialty Company was merged into Follansbee, and the latter incurred expenses of $10,237.85 and of $22,297.82 relating thereto.

The bases of the assets of Follansbee Brothers Company and of Sheet Metal Specialty Company constituted the bases of such assets in the hands of Follansbee. None of said expenses was deductible when paid or incurred, but all were required to be capitalized on Follansbee's books.

REASONS FOR GRANTING THE WRIT

NET LOSS ISSUE

1. In denying to Follansbee-Union Chemical, a single corporate taxpayer, from prior to January 1, 1954 through 1957, a deduction for part of a net operating loss sustained by it in its taxable year that began on January 1, 1954, notwithstanding that control of its stock was not acquired by any person, within the contemplation of Section 269 of the 1954 Code, the decision of the Court of Appeals in this case on the net loss issue is in direct conflict with the decision of the Court of Appeals for the Ninth Circuit in Maxwell Hardware Co. v. Commissioner, 343 F.2d 713 (9th Cir., 1964), on an important recurring question of federal law, and is basically inconsistent with one of its own decisions, with several decisions of this Court, including Central R.R. & Bkg. Co. v. Georgia, 92 U.S. 665 (1876), and with a decision of a District Court from which no appeal was taken.

The decision adverse to Vulcan on the net loss issue was, in terms, based solely upon the application of Section 269 of the 1954 Code. This necessarily carried the implication that Section 172 of that Code would otherwise authorize the deduction (pp. 13a-16a).

In *Maxwell Hardware Company* v. *Commissioner,* 343 F.2d 713 (9 Cir. 1964), two individuals acquired, for cash, non-voting preferred stock in a loss corporation, which entitled them to participate in the benefit of the net loss carryover. The value of the preferred stock was less than the value of stock retained by its former stockholders, so that the new stockholders did not acquire "control" of the loss corporation, as defined by Section 269(a). The loss corporation thereafter engaged in a business different from that conducted by it when the losses were incurred, and such new business produced the income sought to be taxed.

The Ninth Circuit then held that the loss corporation was entitled to take the net operating loss deduction, notwithstanding the provisions of Section 269, held that Section 382(a) did not apply, and refused to apply the rationale of *Libson Shops* v. *Kochler,* 353 U.S. 382 (1957) to a case arising under Section 172 of the 1954 Code. But, in the case at bar, neither Section 382(a) nor *Libson Shops* was relied on by the Court of Appeals or the District Court. See pp. 13a and 14a.

In this case, the stockholders of Follansbee-Union Chemical retained more than 50 percent of its common stock, and received all of its preferred stock. The Court of Appeals called this total 57% of the stock. The preferred stock was issued in order to give them the estimated value of the net loss carryover. This should preclude the application of Section 269(c) of the 1954 Code.

So, contrary to the principle applied in *Maxwell Hardware,* the single corporate taxpayer which was the surviving corporation in the 1954 merger, Follansbee-Union Chemical, was denied its own net operating loss carryover for its taxable year 1957, although "control," thereof as defined in Section 269, was not shifted. This definition reads:

> "For purposes of paragraphs (1) and (2), control means the ownership of stock possessing at least 50 percent of the total combined voting power of all classes of stock entitled to vote, or at least 50 percent of the total value of shares of all classes of stock of the corporation."

The basic conflict between the decision in this case and that in *Maxwell Hardware* lies in the fact that

the latter case requires a change in the ownership of stock which would effect a shift in what we shall call "stock control" while the Court of Appeals, in this case, held, implicitly, that no such change was required. This resulted, primarily, from the treatment of the acquisition of the properties of a corporation as the acquisition of control thereof, notwithstanding the foregoing definition of control.

Indeed, here we have an application of clause (1) rather than of clause (2) of Section 269(a), although it was recognized that clause (2) was the one at issue, p. 10a. The conclusion that there was a shift in the "ownership of a profitable corporation" and therefore of control was rested solely on the acquisition of the properties, not stock, of Consumers and Frontier, e.g., pp. 15a and 16a. A further statement respecting this error is found in the discussion of Reason 3.

In *United States* v. *Jackson Oldsmobile, Inc.*,[4] 371 F.2d 808 (5 Cir. 1967), the Fifth Circuit also gives effect to the same policy respecting the necessity for a change in stock control, for there was about a 40% change in ownership of the net loss carryover. The Court of Appeals distinguished this case on the ground that there was no change in business, p. 14a. But *Maxwell Hardware* treats a change in business as immaterial when there is no shift in stock control, and examination of Section 269 shows that it is indeed irrelevant.

The decision in the case at bar is also in essential conflict with the rationale of several cases decided by

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[4] This decision is erroneously called *United States* v. *Jackson Automobile, Inc.*, on page 14a.

this Court involving exemptions of corporations from various types of state taxation. In those cases, the surviving corporation in a merger has been held to be entitled to its own tax exemptions, notwithstanding the addition of stockholders pursuant to the merger, and a resulting change in the beneficial ownership of the exemptions. The cases include *Central R. R. & Bkg. Co.* v. *Georgia,* 92 U.S. 665 (1876), *Wright* v. *Georgia R. & Bkg. Co.,* 216 U.S. 420 (1910) and *Redwine* v *Georgia Ry. & Bkg. Co.,* 344 U.S. 925 (1953). Other cases are cited in the opinions in those cases. A deduction is not entitled to any more favorable treatment than an exemption. *Central R. R. Co.* v. *Georgia* is also an important authority on the organization expense issues.

There is confusion in rulings, and press releases, by the Commissioner relating to the extent to which this Court's decision in *Libson Shops* is effective under the 1954 Code, and this confusion is illustrated by the decision of the Court of Appeals below. Unless the case at bar is an exception, all the cases which have considered the question, including *Jackson Oldsmobile, Maxwell Hardware* and *WOFAC Corporation* v. *U. S.,* 269 F.Supp. 654 (D.C. N.J., 1967), concur in concluding that a change in business alone, of a single corporate taxpayer, not accompanied by a shift in "stock control," is not significant under Section 172, and is to be taken account of only if required by Section 382 of the 1954 Code. This confusion should be eliminated by this Court as we undertake to show below.

No appeal was taken from the decision in *WOFAC Corporation.* The treatment of T.I.R. 773 in the opin-

ion of the Court of Appeals on page 15a and in footnote 9, page 13a, is inadequate. The Release is cited at the end of the concurring opinion in *Jackson Oldsmobile* to sustain the position which we assert, namely that Section 269 in this context proscribes only a shift of as much as 50% of the beneficial interest in the net loss carryover. (371 F.2d 809) The Release is copied on pp. 37a-39a.

2. The Court of Appeals has decided an important question of federal law respecting the application of Sections 172 and 269 of the 1954 Code which has not been, but should be, settled by this Court, and the substance of which was left undecided in Libson Shops, Inc. v. Koehler, 353 U.S. 382.

This reason corresponds with the reason assigned for granting the writ in *Libson Shops,* 353 U.S. 384. However, that decision left undecided several questions which are presented in the case at bar, and it applied Section 122 of the 1939 Code, while we are concerned here with Section 172 of the 1954 Code. While both deal with net operating loss deductions, there are material differences in the two sections and codes, as conceded in footnote 2 to the opinion in *Libson Shops,* 353 U.S. at 384. We use the expression "single corporate taxpayer" because, in footnote 9 to *Libson Shops,* this Court said:

> "We do not pass on situations like those presented in Northway Securities Co. v. Commissioner, 23 B.T.A. 532; Alprosa Watch Corp. v. Commissioner 11 T.C. 240; A. B. & Container Corp. v. Commissioner, 14 T.C. 842; WAGE, Inc. v. Commissioner, 19 T.C. 249. In these cases, a *single* corporate taxpayer changed the character of its business and the taxable income of one of its enterprises was reduced by the deductions or credits of another." (353 U.S. 390)

Originally, the Commissioner acquiesced in all three decisions. Those acquiescences were later withdrawn and the decisions in *Algoma Tube* and *A. E. C. Container Corp.* have been subsequently reversed because control of the loss corporation was shifted. However, the decisions in *Maxwell Hardware* and *WAGE, Inc.* are in accord with the present view of the Commissioner respecting the application of Section 269(a)(1) of the 1954 Code as set forth in Rev. Rul. 63-40, 1963-1 C.B. 45, and in Treasury Information Release 773. They are also in accord with the decision of the Fifth Circuit in *Libson Shops, Inc. v. Koehler*, *supra*, and *Oldsmobile, Inc.* The concurring opinion in Oldsmobile, 1963 T.I.R. 773, 371 F. 2d 449.

However, examination of Section 269 will indicate that a change in business is not material, and that the occasion for consideration of that matter in *Libson Shops* and *Oldsmobile* was this Court's decision in *Libson Shops*. In *Libson Shops*, this Court did not consider the effect of Section 129 of the 1939 Code, predecessor of Section 269 of the 1954 Code, but based its decision on Section 122 of the 1939 Code. The Government's reliance by the Court of Appeals in Section 269 carries the implication that the net loss carry-over would be otherwise available under Section 172, and that court seems to have been unaware of the possible inconsistency. The confusion which would result is eliminated by this Court.

3. The decision of the Court of Appeals in this case on the net loss issue fails to apply the statutory definition of "control" which is found in Section 269(a) of the 1954 Code, in deciding an important question of federal law and this is in conflict with decisions of this Court that require adherence to statutory definitions, such as 62 Cases of Jam v. United States, 340 U.S. 593, and United States v. An Article of Drug, 394 U.S. 784. In doing so, the Court of Appeals also failed to observe the distinction between the stock and property of a corporation and this failure is in conflict with applicable decisions of this Court, such as Central R. & Bkg. Co. v. Wright, 164 U.S. 327.

As noted, Section 269(a) of the 1954 Code contains this definition of what we call "stock control":

> "For purposes of paragraphs (1) and (2), control means the ownership of stock possessing at least 50 percent of the total combined voting power of all classes of stock entitled to vote, or at least 50 percent of the total value of shares of all classes of stock of the corporation." (p. 32a)

We submit that the Court of Appeals did not follow this statutory definition of control, although, at one point, it speaks of the acquisition of a "controlling stock interest in the corporation," (p. 11a) and at another, it says that the inquiry is whether "there has been an acquisition of control as contemplated by Section 269 . . .." (p. 13a). However, the first of these recognitions of the issue is qualified by the statement in footnote 9 that the question is not the "*amount* of stock ownership change, but the *effect* of the change upon control." This is squarely contradictory of the statutory definition, and therefore conflicts with this Court's decisions of the import that statuory definitions shall govern in the construction of a statute. *62 Cases of Jam* v. *United States,* 340 U.S. 593, 596 (1951), and *United States* v. *An Article of Drug,* 394 U.S. 784 (1969).

Instead of following the statutory definition, the opinion in the Court of Appeals treats the acquisition of the *properties* of Consumers and Frontier as involving what is said to be at one place "a substantial change in the ownership of a profitable corporation," (p. 14a). Again, it is said, ". . . there was a shift of 57 percent of the ownership of a profitable corporation." This is followed by the statement that, ". . . considering solely the question of 'control,' we are persuaded that there was an acquisition of the control, under section 269, of profitable corporations. . . ." Again, the Court of Appeals speaks of "Follansbee's acquisition of the chemical and buildings materials companies . . . ." (p. 16a)

Thus, the Court of Appeals fails to observe the well defined distinction between the stock of a corporation and its properties. That Congress intended for its definition of stock control to govern all decisions under Section 269(a) is further shown by the fact that clause (2) thereof deals specifically with the acquisition of property, through the merger process (and possibly others) (p. 32a). Thereby, it necessarily excludes the application of the "stock control" test to an acquisition of corporate property rather than corporate stock. This failure conflicts with the rationale of several cases in this Court, of which *Central R. R. and Banking Co.* v. *Wright,* 164 U.S. 327 (1896), is an instance.

The stipulation of the issues included one as to whether the 1954 net operating loss of Follansbee and "one incurred by Union Chemical in the taxable period January 1 to February 28, 1955, are allowable under Sections 172 and 269(a)(2) in those periods and in taxable years of Follansbee preceding such periods, and subsequent taxable years of Union Chemical . . ." Thus,

the stipulation called for a decision under clause (2), while the Court of Appeals rested its conclusion upon an acquisition of control under clause (1). A corresponding limitation of the issues was included in the amended pre-trial order.

That there was such a limitation of issues is adequately shown in the opinion in the District Court which is directed towards Section 269(a)(2). (308 F. Supp. 56, 58, 59.) The opinion of the Court of Appeals also undertakes to deal with clause (2), apparently without recognition of the fact that it involves the acquisition of property of a corporation in a non-taxable reorganization, such as a statutory merger, and not with the acquisition of "stock control" thereof. One obvious effect of the stipulation is a concession by the Government that there had been no shift of control within the contemplation of clause (1). It has not been suggested that the stipulation was improvidently entered into so as to relieve the Government of the burden of its commitment. In such a case, the stipulation should be observed, *General Utilities & Operating Co.* v. *Helvering,* 296 U.S. 200 (1936).

The main reliance of both courts in arriving at these conclusions was the decision in *Southland Corporation* v. *Campbell,* 358 F.2d 333 (5 Cir., 1966). In that case, however, a loss corporation, Caribbean did acquire "stock control" of a profit corporation, Old Cabell's, and it was therefore possible to invoke clause (1). Actually, the opinion in *Southland Corporation* contains useful statements of the import that Section 269 "is applicable only in certain carefully circumscribed situations," followed by recognition that there must be not only a shift in stock control, but also the proscribed purpose. 358 F.2d at 336. All of these facts are noted in the opinion (p. 12a, including footnote 8).

ORGANIZATION EXPENSE ISSUES

4. The availability of a deduction for organization expenses in consequence of the 1957 merger presents an important recurring question of federal law, on which the decision of the Court of Appeals is in conflict with the decision of this Court in Marr v. U.S., 268 U.S. 536, in essential conflict with the decision of the Court of Appeals for the Fourth Circuit in Fidelity Baltimore National Bank v. U.S., 328 F. 2d 953, and decisions of other Courts of Appeals and in essential conflict with a decision of a District Court from which the United States did not appeal.

In view of decisions of three Courts of Appeal, the Court of Claims, and decisions of the Board of Tax Appeals in which the Commissioner of Internal Revenue ultimately acquiesced (some cited below), the Government conceded, in the Court of Appeals, that organization and reorganization expenses of the nature here involved may be deducted "upon the dissolution and liquidation of a corporation" (p. 6a). The Court of Appeals also recognized that the "separate existence of all the constituent corporations . . . except the one into which the other or others of such constituent corporations have been merged" ceased, under the controlling provisions of the Delaware statute, 8 Del. Code Anno. 259(a) (p. 7a confirmed on p. 8a). The full text of this section of Delaware law is copied on p. 26a.

Therefore, we forego citing any of the numerous cases that hold to that effect except some that are also relevant to other phases of the cases, such as *Central R. R.* v. *Georgia,* 92 U.S. at 672 and 674. The Court of Appeals then undertook to show that there was a difference between the termination of corporate existence which follows dissolution and that which follows merger. That Court said,

> "In a dissolution, the privileges, *powers, rights* and duties of the corporation come to an end and

> suffer a corporate death. In a merger, these attributes of corporate life are transferred to the surviving corporation and are there continued and preserved." (p. 8a, emphasis supplied)

In spite of this fairly clear statement and of the implications of the quotation from the Delaware statute, the Court of Appeals includes a quotation from Fletcher, Cyclopedia of Corporations (Perm. Ed.) which does not make it clear that the corporate life of the non-surviving constituent corporation is terminated, and that it is dissolved (p. 7a, quoting from 15 Fletcher, Cyclopedia of Corporations § 7041). Fletcher contains inconsistent statements about the effects of mergers and consolidations and is not, therefore, wholly reliable. In Section 7079, there is an unequivocal statement that supports the position which we advance in respect of this effect of a corporate merger under statutes like the Delaware statute:

> "The statute may be so worded as to leave one or all of the constituent corporations in existence, at least for a limited time, or it may expressly or impliedly provide for the absorption of one company by the other, the *former going out of existence* and the latter remaining in existence, which constitutes a merger rather than a consolidation; . . . ." (15 Fletcher 94-5, emphasis supplied)

While the opinion of the Court of Appeals shows that Follansbee-Union Chemical was a Delaware corporation, it does not disclose that Vulcan, the survivor in the 1957 merger, is a New Jersey corporation (p. 4a). So there is no independent discussion of the significance of that fact.

The foregoing statement of the assumed effects of a merger are in direct conflict with the decision of this Court in *Marr* v. *U.S.*, 268 U.S. 536 (1925). This in-

volved a change in the domicile of a New Jersey corporation to Delaware through acquisition of stock by the Delaware corporation and dissolution of the New Jersey corporation. In holding that this gave rise to taxable income prior to the adoption of statutes which do not tax profits realized in reorganizations of that character, this Court said, "In the case at bar, the new corporation is essentially different from the old. A corporation organized under the laws of Delaware does not have the same *rights* and *powers* as one organized under the laws of New Jersey." (268 U.S. 541, emphasis supplied)

Plainly, the result reached by the reorganization process involved in *Marr* is the same as would have been reached by a statutory merger of a New Jersey into a Delaware corporation. *Central R. & Bkg. Co.* v. *Georgia,* 92 U.S. at 673, copied in the argument. There were also some changes in relative stock ownerships which led this Court to observe that the stockholders of the New Jersey corporation did not have "the same proportional interest of the same kind in essentially the same corporation." (268 U.S. 541)

Obviously, this is true in the case of the 1957 merger of Union Chemical into Vulcan and of mergers generally. Plainly, the stockholders of Follansbee-Union Chemical wound up with a stock interest in a corporation which was totally different from their prior stock interest in a different corporation owning different assets. The first of the foregoing statements in the opinion in *Marr* is expressly relied on in two decisions involving the imposition of stamp taxes, namely, *U.S.* v. *American Vortex Cup Co.,* 84 F.2d 925, 927 (7 Cir., 1935), and *Jefferson Lake Sulphur Company* v. *U.S.,* 195 F.2d 1012, 1015 (5 Cir., 1952).

Essentially the same conclusions were reached in *Fidelity Baltimore National Bank* v. *United States,* 328 F.2d 953 (4 Cir., 1964), involving liability for stamp transfer taxes on the "consolidation" of a state bank with a national bank under the charter of the latter. This was found to be essentially a merger. The Fourth Circuit expressly commented on the difference in jurisdictions involved, 328 F.2d at 956-7.

Marr and *Fidelity-Baltimore* dispose of the questions of transmission of "rights" and "powers." But it is equally plain that corporate "duties" are not transmitted to the surviving corporation organized in another state, at least to any greater extent than in the case of any other assumption of liabilities. For example, Vulcan is not obligated to pay Delaware franchise taxes. It has its own "duties," and so did Follansbee-Union Chemical after the 1954 merger. In *Fidelity Baltimore,* the Fourth Circuit noted that the merged corporation does not file income tax returns, 328 F.2d at 958.

Aside from the Fourth Circuit in that case and the Fifth Circuit in *Jefferson Lake Sulphur Co.,* which may not have involved a statutory merger, Courts of Appeals of three other circuits have imposed stamp transfer taxes on the non-surviving constituent corporation in a corporate merger, namely *U. S. Industrial Chemicals Inc.* v. *Johnson,* 181 F.2d 413 (2 Cir. 1950); *American Processing & Sales Co.* v. *Campbell,* 164 F.2d 918 (7 Cir., 1947), cert. den. 333 U.S. 844 and *Emporium Capwell Co.* v. *Anglim,* 140 F.2d 224 (9 Cir., 1944) cert. den. 322 U.S. 752. These were based on the essential nature of a statutory merger, namely that the assets of the non-surviving constituent (generally,

and hereafter called the "merged corporation") are transferred to the surviving corporation in consideration of the issue of stock of the latter, and the assumption of the former's liabilities.

These, and other cases, necessarily proceed on the assumption that the corporate existence of the merged corporation is terminated and that its franchise to be a corporation is not transferred. Two other cases in other circuits that proceed on the same hypothesis are cited because they involve Delaware corporations, *Koppers Coal & Transportation Co.* v. *U.S.*, 107 F.2d 706 (3 Cir., 1939), and *Jones* v. *Noble Drilling Co.*, 135 F.2d 721 (10 Cir., 1943).

Finally, in *Dragon Cement Co.* v. *U.S.*, 144 F. Supp. 188 (D.C. Me., 1956), an organization expense was expressly allowed as a deduction, and it is in direct conflict with the decision in the case at bar. While the Government appealed from this adverse judgment, it was only on another aspect of the case. *United States* v. *Dragon Cement Co.*, 244 F.2d 513 (1 Cir., 1957). This conflict and the fact that this issue presents a recurring problem in the law of federal income taxation should influence this Court to review these cases on this issue.

The decision in *Dragon Cement* appears to have been the reason why the District Court thought that expenses of qualifying to do business in Illinois might be deductible and for what may have been a similar concession by the Court of Appeals. (308 F. Supp. 58, 59, p. 9a, f.n. 4) The Court of Appeals summarized its conclusions with the statement that the "capital assets" here involved "were not *lost*, but were continued beyond the corporate existence of the constituent corporations and

persisted as capital assets of the surviving corporation" (p. 9a, emphasis supplied).

We submit that this conclusion is essentially incorrect as to certain other items of expense such as those involving the capital structure, and is not in accord with applicable decisions. Of these, the most significant are *Union Chemical & Materials Corp.* v. *Cannon,* 38 Del. Ch. 203, 148 Atl. 2d 348 (Del. Sup. 1959); *Central R. Co.* v. *Georgia;* and *Rochester R. Co.* v. *Rochester,* 205 U.S. 236 (1907). However, since the question also arises in the case of the 1954 merger, we discuss it in that connection. So also with the effects of the correspondence of the "end result" in the case of a corporate merger and a "C" type reorganization. The quoted words come from the opinion in *American Processing and Sales Co.,* 164 F.2d at 920.

The predicates on which the stamp tax cases are decided establish that there is a liquidation as well as a dissolution of the merged corporation. Since it supplies the consideration, it is entitled to the rights to the stock of the surviving corporation and, in effect, transfers them to its stockholders. By having this stock issued to its stockholders, it divests itself of all of its assets upon the consummation of the merger and thus effects the substance of a liquidation concurrently with its dissolution. Cf., *Rochester R. Co.* v. *Rochester.*

In the final analysis, the decision below is rested on the decision in *Citizens Trust Co.* v. *Commissioner,* 20 B.T.A. 392 (1930), which is cited in the opinions of both the Court of Appeals and the District Court (308 F. Supp. 56, and p. 9a). In the argument, we undertake to show that this case is based on a misconception of the law of New York.

5. The decision of the Court of Appeals in this case on the organization expense issue involved in the 1954 merger is in essential conflict with the rationale of several decisions of other Courts of Appeals, including that of the Seventh Circuit in American Processing and Sales Co. v. Campbell, 164 F. 2d 918, and derivatively, with this Court's decision in Raybestos-Manhattan, Inc. v. United States, 296 U.S. 60 and with that of the United States Tax Court in Kingsford Company v. Commissioner, 41 T.C. 646, in which the Commissioner has acquiesced.

Here, we are primarily concerned with the essential nature and effects of a corporate merger described above, but deal only with a single state. It is not important that the stock is issued direct to the stockholders of the merged corporation. Cf., *U.S.* v. *Vortex Cup Co.* and *Raybestos-Manhattan, Inc.* v. *U.S.*, 296 U.S. 60 (1935).

What is important is that, in the process, the stock of the merged corporation ceases to have any intrinsic value, just as in the case of the stock of a dissolved corporation that has completed its liquidation. This is due to the fact that the stock of the merged corporation ceases to represent an interest in property, since not only is it dissolved, but also the transferable property of the merged corporation has vested in the surviving corporation. Therefore, it is the stock of the latter corporation which evidences interests in that property and, of course, in its own retained property.

So, the value of expenditures related to the issue of stock of the merged corporation is "lost," the criterion applied by the Court of Appeals in this case (p. 9a). Such expenditures create what may be called the "capital structure" of the merged corporation. This capital structure is not continued beyond the corporate existence of the merged corporation, and therefore does

not persist as a capital asset of the surviving corporation, as required by the Court of Appeals (p. 9a).

That such is the case is, we submit, conclusively established by the decision of the Supreme Court of Delaware in *Union Chemical* v. *Cannon, supra,* since it considered the effect of the 1957 merger on the stock of Union Chemical. The Delaware Supreme Court held that the shares of Union Chemical were "automatically converted into shares of Vulcan" and so could no longer support jurisdiction by attachment (38 Del. Ch. 206, 209, 148 Atl. 2d 351). The effect on the shares of capital stock of the mergers there involved were significant influences in the decisions of this Court in *Central R. R.* v. *Georgia,* 92 U.S. at 672 and *Rochester R. Co.* 205 U.S. at 256. In the latter case, it was said that dissolution resulted because the corporation was left "without stock, officers, property or franchises."

Certain specific expenditures relating to the original issue of the capital stock of Consumers, the value of each of which was surely lost upon the consummation of the merger of Consumers into Follansbee-Union Chemical, are listed beginning at page 43a of the appendices. In addition to those, the compensation of committees for creditors or stockholders, of counsel therefor, and for individual creditors or stockholders, and certainly the bulk of the compensation for the trustees and their counsel related to the creation of the capital structure of Consumers which was obliterated by its merger into Follansbee-Union Chemical. Therefore, the value thereof must have been "lost" upon the consummation of that merger.

If because both of these were Delaware corporations, the deduction is not available but would be available upon the merger of Follansbee-Union Chemical into

Vulcan, then the reasoning stated above would also be applicable. The foregoing reasoning is also applicable to the reorganization expenses of Falkenau Brother Company and of Falkenau Metals, which were involved in the 1957 merger.

The organization expenses should be also allowed as a deduction in the case of the 1956 merger because a statutory merger accomplishes the same "end result" as does a "C" type reorganization in which the transferee assumes the liabilities of the transferor and the transferor is promptly liquidated. A "C" type reorganization is defined in paragraph (C) of section 368(a)(1) of the 1954 Code and involves essentially "the acquisition by one corporation in exchange solely for all or a part of its voting stock of substantially all of the properties of another corporation," which may be forthwith distributed. In *Commissioner* v. *Commissioner*, 41 T.C. [illegible] (1964), 1964-1 Cum. Bul. 6[illegible], the deduction of organization expenses was allowed in a "C" type reorganization. This was true also in the case of *Pacific Coast Biscuit Co.* v. *Commissioner*, 32 BTA 30[illegible] (1935), 1935-1 Cum. Bul. 19[illegible]. The latter is one of the cases which the Government conceded was correctly decided [illegible].

The decision in one of the stamp tax cases, *American Processing & Sales Corporation*, was in part specifically rested on the proposition that since the "end result" of a statutory merger was the same as the procedure involved in *Bayberry Corporation, Inc.*, the stamp tax consequences should be the same. The Court said on this subject:

> "Forms are not important. It is the end result that counts. The end result is the same in both cases." (164 F.2d at 920)

Raybestos Manhattan, Inc. involved what was, in fact, a "C" type reorganization in which the assets of one corporation were transferred to another with the stock of the transferee being issued direct to the stockholders of the transferor. Therefore, we urge that the decision of the Court of Appeals is essentially in conflict with that decision of this Court.

6. The decision of the Court of Appeals involves important recurring questions of federal law relating to the deductibility of expenses of organization and reorganization upon the consummation of a statutory merger of one corporation into another which have not been, but should be, decided by this Court.

Although the adoption of Section 248 of the 1954 Code may reduce the amount of organization expenses which may be claimed as a deduction upon the consummation of a statutory merger, this statute is not deemed to apply to reorganization expenses. Nor does it apply to any organization expenses which were incurred before the adoption of the 1954 Code. Therefore, the question of the deductibility of organization and reorganization expenses of the non-surviving constituent corporation will arise upon the consummation of most, if not all, statutory mergers.

Either as the result of a decision by a Court of Appeals, as in *Bryant Heater Company* v. *Commissioner,* 231 F.2d 938 (6 Cir., 1956), and *Gravois Planing Mill* v. *Commissioner,* 299 F.2d 199 (8 Cir., 1962), or by the Court of Claims, as in *Koppers Company, Inc.* v. *U.S.*, 278 F.2d 946 (1960), or of acquiescence by the Commissioner, as in *Kingsford Company,* taxpayers have been allowed deductions for the organization and reorganization expenses in other types of non-taxable exchanges than statutory mergers, including reor-

ganizations, notwithstanding that the "end result" is often substantially the same. The effect is an emphasis upon form rather than substance. *Bryant Heater* and *Koppers Company* are two of the decisions which the Government conceded were correctly decided (p. 6a).

Since the issue will frequently be presented because of the numerous statutory mergers that take place in the United States and since there is plain discrimination against the corporate statutory merger form, this Court should determine the constantly recurring federal questions that are presented in this case on the organization expense issues.

ARGUMENT

Net Loss Issue

As we have noted, the decision of this Court in *Central R. R.* v. *Georgia,* is significant in the decision of all of the issues presented by this petition. That case involved what was held to be a merger of one Georgia corporation into another under a special statute. It was held that an exemption from certain types of taxation given to the surviving corporation was retained by it after the consummation of the merger, although stockholders of the non-surviving constituent received stock in that survivor.

However, the exemption was held not to apply to property acquired from the non-surviving constituent, which this Court held had ceased to exist (92 U.S. at 672 and 674). The concise statement of the substance and effect of a merger which this Court there employed reads:

> "At most, it intended a merger of the Macon and Western Railroad Company into the other, a mode

> of transfer of that Company's franchise and property and a payment therefor with stock of the Central Company." (92 U.S. at 673)

The holding that the surviving corporation was entitled to a similar tax exemption in a merger is the subject of several other decisions of this Court, some cited in the above opinion. However, we have noted only decisions involving such exemptions under Georgia law because they are much more recent cases. *Wright* v. *Georgia R. & Bkg. Co.,* 246 U.S. 420 (1910), and *Redwine* v. *Georgia R. & Bkg. Co.,* 344 U.S. 925 (1953), following it, both cited above. Thus, in the absence of a constitutional statute preventing it, the single continuing corporations were held to be entitled to an exemption from taxation notwithstanding some change in the beneficial ownership thereof. A deduction is entitled to no less favorable treatment than an exemption.

Beginning on p. 39a of the Appendices, we include extracts from reports of the Ways & Means Committee of the House of Representatives and of the Senate Committee on Finance to show the legislative history of relevant portions of the 1939 and 1954 Codes.

It is quite common to say that Section 129 of the 1939 Code, the predecessor of Section 269 of the 1954 Code was adopted to prevent so-called "trafficking" in net operating loss deductions. However, the statute is not confined to those deductions and in *Maxwell Hardware,* the Ninth Circuit stated that this is a "question-begging epithet which clouds reason." It then declared that consideration of the 1954 Code must lead to the conclusion that "Congress has deliberately sanctioned such 'trafficking' in those situations where it is

not expressly abjured." (343 F. 2d 719) See also 343 F. 2d 718.

Maxwell Hardware stands for the proposition that there must be both a change in stock ownership of the *loss* corporation to the required extent, and the existence of the proscribed tax avoidance purpose—the latter alone is not sufficient. (343 F. 2d 719-21) The necessity that a tax cannot be imposed unless all conditions precedent are met is in accord with the decision in *Crooks* v. *Harrelson,* 282 U.S. 55 (1930). This case also applied the principle that tax statutes are to be strictly construed.

The Tax Court in *Maxwell Hardware,* reported *sub nom, Arthur T. Beckett,* 41 T.C. 413-4, had also required that both conditions be met. While it found that the tax avoidance purpose existed, it had held Section 269 to be inapplicable because there had not been the required shift in stock ownership. The Court of Appeals concurred though the Government sought to have Section 269 applied.

Therefore, the decision of the Tax Court was based upon the application of the doctrine of *Libson Shops,* because of the change in business. (41 T.C. 414-6) The Ninth Circuit rejected this conclusion upon a full examination of the issues and with specific reference to the differences between Section 172 of the 1954 Code and Section 122 of the 1939 Code and the inclusion of Sections 381 and 382 in the 1954 Code (343 F. 2d 715-9). So, that court concluded that Congress intended to "countenance 'trafficking' in operating loss carryovers" subject to the limitations of Sections 381 and 382. Section 269 was treated separately in the manner shown above. (343 F. 2d 718)

The adoption of Section 381 and Section 382(b) are significant, because Section 381 specifically permits the enjoyment of net operating loss deductions by the survivor in a non-taxable reorganization such as is accomplished by a statutory merger. Furthermore, under Section 382(b), the stockholders of the loss corporation need to procure only 20% of the stock of the surviving corporation in order for the surviving corporation to obtain the full benefit of the deduction (p. 36a).

It would indeed be an anomaly for the Court to hold that, for example, Consumers would be entitled to the net operating loss deduction of Follansbee if Consumers rather than Follansbee had been the surviving corporation. Yet, that result seems to be clear under Sections 381 and 382, and it would be illogical for the Court to hold that what is there specifically granted, is taken away by Section 269. See *62 Cases of Jam* v. *U.S.*, 340 U.S. at 599-600.

The Ninth Circuit emphasized the finding of the Tax Court that *Maxwell Hardware* was a taxable entity and was the entity which had suffered the losses as well as generated the income sought to be taxed. (343 F. 2d 717) In this respect, the case at bar is identical with that presented in *Maxwell Hardware*. The Ninth Circuit also rejected the view that a mere change in business required disallowance of the deduction either under Section 172 or Section 382 (343 F. 2d 717, 720). But Follansbee Union Chemical is just as much the same corporation, after the merger, as was *Maxwell Hardware* after the sale of some additional stock.

Other provisions in the 1954 Code and its legislative history are persuasive that the single corporate tax-

payer, Follansbee-Union Chemical, was entitled to the benefit of its own net operating loss carryover, since control was not shifted. Section 172(d)(4)(A) gave the benefit of net operating loss deductions to individuals in the case of a sale of operating assets (p. 31a). They had denied that under the 1939 Code on the theory that this was not a loss sustained in the conduct of a business. No amendment was deemed to be necessary to give this treatment to corporations, since the Committee Reports included this parenthetical statement:

> "(Corporations are entitled to this treatment under present law and under this section.)"

This statement and its context are copied in Item 1, p. 40a. This statement includes, in effect, a legislative construction of the 1954 Code which should be given effect. *Helvering* v. *Twin Bell Oil Syndicate,* 293 U.S. 312, 322 (1934).

Again, Section 382(b)(1) includes a provision which makes it clear that the benefits of Section 381 shall be available to either "the transferor corporation or the acquiring corporation" which has a net operating loss carryover (p. 36a). Obviously, no such deduction would be available unless Section 172 were applicable. Here, Follansbee-Union Chemical is the acquiring corporation.

There is nothing in Section 269(a) which justifies a conclusion that clause (1) proscribes the acquisition of property for stock, rather than cash, unless there be a shift in "stock control," as is required by *Maxwell Hardware.* Clause (2) presents a different question to be promptly considered.

We have noted that *Southland* did involve the acquisition of "stock control" of a profitable corporation

by a loss corporation, within the definition of "stock control." However, here, Follansbee-Union Chemical acquired the *properties* of profitable corporations, not their stock. But, in *Southland,* it was held that the acquisition of the property of the profitable corporation upon its merger into the loss corporation released the transaction from the operation of Section 269(a), because the former was "controlled" by the stockholders of the latter. Thus, the same policy of giving to a corporation the benefit of net loss carryovers unless there is a shift in "stock control" is observed.

That there is a difference between the stock of a corporation and its properties is shown by the decision in *Central R. R.* v. *Wright* involving the same exemption statute as that involved in the litigation of that railroad against the State of Georgia. In the later case, this distinction was observed in the holding that municipal corporations could tax the property of the Central Railroad but not its stock, 164 U.S. 335-6.

The reason for the failure of the Court of Appeals to give effect to the statutory definition of "stock control" is not stated in that Court's opinion, and is, we submit, inexplicable and unwarranted. Here, as in *Central R. R.* v. *Wright,* the fact that both subjects, that is the corporate stock and corporate property, are dealt with in the same statute should be significant to influence this Court not to apply clause (1) except in those cases where corporate stock, not corporate property, is acquired by a "loss" corporation.

Since the taxpayer prevailed in *Southland,* the conclusion that the proscribed purpose exists when a "loss" corporation acquires control of a profitable corporation is a mere dictum. The conclusion is based on the decision in *F. C. Publication Liquidating Corp.*

v. *Commissioner,* 304 F. 2d 779 at 781 (2 Cir., 1962), cited on pp. 15a and 16a.

We submit that the cases cited by the Second Circuit do not support the conclusion expressed. Two cases involved multiple corporation situations. All the others involved acquisitions of "stock control" of loss corporations. Furthermore, the conclusion that the "loss" corporation acquired control of the profitable corporation is in direct conflict with the finding and opinion of the Tax Court on that issue. *F. C. Publication Liquidating Corp.* v. *Commissioner,* 36 T.C. 836 at 848 and 851 (1961). In addition, the facts as to earning power and assets appear to require the conclusion that the Tax Court finding was correct, and the Court of Appeals' conclusion incorrect (36 T.C. at 837 and 847).

The conclusions of the District Court and of the Circuit Court that the proscribed purpose existed might be considered to present a non-reviewable question of fact except that each is based upon an unjustified legal conclusion as to what constitutes "evasion or avoidance of Federal income taxes." Here, the Court of Appeals relied upon the opinion in *Southland* to conclude that Section 269 "is applicable when a 'loss' corporation acquires control of a 'profitable' corporation, since the acquiring corporation thereby secures the benefit of a loss it would not have otherwise enjoyed." (358 F. 2d at 336, copied on p. 15a) The assertion of this view of that part of Section 269 which deals with the principal purpose of tax "evasion or avoidance" is truly misplaced (p. 32a).

The effect of it is to withhold a deduction expressly provided for by statute, namely, in Section 172, if the

single corporate taxpayer which suffered the loss there involved procures *income producing* property by some means. Otherwise stated, it means that a corporate taxpayer does not "enjoy" the "benefit" of a deduction to the extent that it does not have gross income to absorb *all* of the available deduction. That such a result is not contemplated by the statutory scheme is made clear by recognition of the fact that there would be no such thing as a net operating loss on such a theory, for a net operating loss is merely the "excess of the deductions allowed by this chapter over the gross income." (Section 172(c), p. 31a)

In the Court of Appeals, we urged that the permanent investment of some $8,500,000 was a more important purpose than the possible recovery of only $2,300,000. The Court of Appeals disagreed with us, but it was acting under a misapprehension as to the full contents of the entire Proxy Statement. While we urge that the existence of such a proscribed purpose is not conclusive in the absence of the required shift in stock control, we have added material at the end of the appendices to show that the Court of Appeals acted under such a substantial misapprehension. There are statements in the opinion which rather indicate that, if the relationship between the sale of Follansbee operating assets and the merger had been as the Proxy Statement demonstrates they were, the decision might have been favorable to Vulcan on the issue of the proscribed purpose. See p. 44a.

While the decision below is surely based upon a misapplication of clause (1), it appears appropriate to demonstrate that clause (2) would not operate to prevent the deduction by Follansbee-Union Chemical of its own net operating loss carryover. This results

from the fact that clause (2) most plainly deals only with deductions based on, or attributable to, the properties acquired in a non-taxable transaction and not with a deduction to which a single corporate taxpayer had always been entitled. That subject is not discussed in the opinion below.

That conclusion is indicated most definitely by the inclusion, in clause (2), of the requirement that the basis of the property acquired from a corporation "in the hands of the acquiring corporation is determined by reference to the basis in the hands of the transferor corporation. . . ." (p. 32a) The evil to which this part of the statute was directed was the acquisition of property having a high basis at a time when its value was low. As a result, the acquiring corporation could procure a deduction for depreciation or a loss on the sale of the property substantially higher than would be permissible if based on the value of the consideration paid by the acquiring corporation in the acquisition.

The concept of Section 269 was introduced into the law by Section 122 of the Internal Revenue Act of 1943, adding Section 129 to the 1939 Code. Regulations were issued thereunder in Treasury Decision 5426, issued on December 29, 1944 (1945 C.B. 196) and remained in effect until 1962. The only specific dealing in those regulations with clause 2 reads as follows:

> "(c) If the requisite *acquisition* and purpose exist, among the transactions within clause (2) of Section 129(a) is the following: A corporation acquires property having in its hands a *substituted* basis which is *materially greater than its fair market value* at the time of such acquisition in order to secure a larger excess profits credit or

> to utilize the property to create tax-reducing losses." (§ 29,129-3(c) of Reg. 111, § 39.129-3(c) of Reg. 118, emphasis supplied)

That this illustration was in accord with Congressional intention is shown by the legislative history of Section 269. Item 4 in the Appendices, p. 42a, contains extracts from the Committee Reports of both the House of Representatives and the Senate. Possibly, the most significant portion of that legislative history is the following sentence:

> "Disparities of this type generally arise where the old basis is continued in the hands of the new owner."

But no challenge is made to any deduction with respect to the property acquired from Consumers and Frontier in reliance upon Section 269. So clause (2) is plainly inapplicable.

Organization Expense Issue

The case which originally introduced the concept that organization expenses should not be allowed as a deduction in the case of a merger, although allowable in the case of dissolution, is *Citizens Trust Company,* 20 BTA at 393. All subsequent statements of that import are based, in the final analysis, on that decision, and the Court of Appeals copied an extract from the opinion therein as follows:

> "It has been said that 'all "rights, powers, liabilities and assets" [survive] except the "indicia and attributes of a corporate body distinct from that into which it is merged."'" (p. 8a-9)

The foregoing statement is based upon an extract from *McKinney's Consolidated Laws of New York,*

Vol. 4, p. 402, which is copied in the opinion in *Citizens Trust*. The words which are copied in that opinion come from the opinion in *Bank of Long Island v. Young*, 101 Appel. Div. 44, 91 N.Y.S. 1047 (1905). But this case involved a totally different issue, namely whether the surviving bank would remain on an obligation of guaranty owing to the merged bank.

That the conclusion expressed in *Citizens Trust* does not represent the law of New York is indicated by the decision of the highest court of that state in the case of *In Re Bergdorf's Will*, 206 N.Y. 308, 99 N.E. 715 (1912) ("*Bergdorf's case*"). It was therein held that the merged trust company did not exist within or as a part of the surviving trust company and that except as its corporate existence was continued to permit suits against it, it was non-existent. In support of this conclusion, the New York Court of Appeals cited numerous cases, including *Central R. R.* [illegible] and two other decisions of this Court. Again the New York Court of Appeals said that for all of the purposes of the consideration there involved, the merged corporation ceased to exist when the merger was accomplished (206 N.Y. 315-6, 99 N.E. 717).

The New York statute provided that the surviving corporation should hold and enjoy "all rights of property, franchises and interests, etc." in the same manner as the merged trust company. But in *Bergdorf's case*, the New York court stated that this meant that every right of the merged company ("except the right to be a corporation") was to pass to the surviving trust company (206 N.Y. 315, 99 N.E. 717).

Since *Citizens Trust Company*, and decisions following it, including that of the Court of Appeals in the

case at bar, are based upon an erroneous view of the law of New York and enunciate a theory which is in conflict with the decisions of this Court respecting corporate mergers, it should be specifically rejected as an authority in dealing with the deductibility of organization and reorganization expenses upon the consummation of such a merger.

Furthermore, the discrimination against reorganizations and other non-taxable transactions in different forms should be eliminated. By quotation from the opinion in *Central R. R.* v. *Georgia,* 92 U.S. at 673, we have called attention to the fact that a merger involves a transfer of the property of the merged corporation in consideration of the issue of stock of the survivor to the stockholders of the former. Transfers of the property of one corporation for stock in another pose a constitutional problem under *Dartmouth College* v. *Woodward,* 4 Wheaton 518.

This, no doubt, is the reason for the inclusion of dissent provisions in merger statutes, e.g., *Central R. R.* v. *Georgia,* 92 U.S. at 671-2, *Mason* v. *Pewabic Mining Co.,* 133 U.S. 50 (1890), but it was a type of transaction commonly used before the adoption of statutes authorizing the sale of all of the property of a corporation, even for cash. Thus, a statutory merger accomplishes the same "end result" as does a reorganization in pursuance of paragraph (C) of Section 368(a)(1) of the 1954 Code when the stock of the transferee is promptly distributed. The transferee may assume the liabilities of the transferor without impairing the non-taxability of the reorganization.

Therefore, the income tax consequences should be the same with respect to the deductibility of organiza-

tion and reorganization expenses. See *American Processing & Sales Company,* where cited just before the argument, 164 F. 2d at 920.

CONCLUSION

The decision of the Court of Appeals deals erroneously with at least two matters of importance in the federal income tax field which may be expected to recur constantly. We respectfully request that the writ of certiorari be issued.

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